Supreme Court, U.S.
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No. 96-964

In The

Supreme Court of the United States

October Term, 1996

AMERICAN LIFE & CASUALTY INSURANCE COMPANY,

Petitioner,

v.

ANNE C. TROSTEL, et al.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Eighth Circuit

REPLY BRIEF FOR THE PETITIONER

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REPLY BRIEF FOR THE PETITIONERS[1]

1. Respondents' opposition to certiorari confirms, unwittingly, that the amendment to Section 5118(d)(2) enacted by Congress on September 30, 1996, had the specific effect of reversing the Eighth Circuit's decision in this case. Respondents emphasize that this case is "factually and legally indistinguishable" from the two cases on which the Eighth Circuit exclusively relied – *Fay Corp. v. BAT Holdings I, Inc.*, 646 F. Supp. 946 (W.D. Wash. 1986), *aff'd sub nom. Fay Corp. v. Frederick & Nelson Seattle, Inc.*, 896 F.2d 946 (9th Cir. 1990), and *Wells Fargo Bank v. Bank of Am.*, 38 Cal. Rptr. 2d 521 (Cal. App. 1995). Opp. at 6-8. Specifically, Respondents stress that here, as in *Fay Corp.* and *Wells Fargo Bank*, the Court of Appeals held that a post-1977 assignment of a pre-1933 lease containing a gold clause constituted a "novation" of the lease agreement and thus "revived" the previously unenforceable gold clause under Section 5118(d)(2) which at the time of the Eighth Circuit's decision permitted enforcement of gold clause obligations "issued after October 27, 1977." 31 U.S.C. § 5118(d)(2).

Less than two months after the decision below was announced, however, Congress enacted an amendment to Section 5118(d)(2) specifically designed to overrule the *Fay Corp.* and *Wells Fargo Bank* cases. Responding particularly to the "unfair treatment to lease holders" reflected in those cases, 142 Cong. Rec. H4755 (May 7, 1996), Congress amended Section 5118(d)(2) to make clear that a post-1977 assignment or novation of a pre-1977 obligation

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[1] Petitioner's Rule 29.6 Statement appears at Petition for a Writ of Certiorari at ii.

containing a gold clause does not revive the gold clause *"unless all parties to the assignment or novation specifically agree to include a gold clause in the new agreement."* Pub. L. No. 104-208, § 2609 (emphasis added).[2]

The Eighth Circuit's holding in this case vividly illustrates the "unfair treatment to lease holders" that motivated Congress to enact the 1996 amendment to Section 5118(d)(2). The lease at issue here has been controlled by Petitioner's corporate parent, The Statesman Group ("Statesman"), since 1969, when another entity under Statesman's control, State Automobile and Casualty Underwriters ("State Auto"), acquired the lease through an assignment from an unrelated entity. In December 1985 State Auto assigned the lease to Statesman, and in August 1990 Statesman assigned the lease to Petitioner, its wholly owned subsidiary. It is undisputed that State Auto's 1985 assignment of the lease to Statesman, and Statesman's 1990 assignment of the lease to Petitioner, were effectuated for reasons wholly internal to the organization. Indeed, Respondents were not signatories to, or otherwise involved in, the 1985 and 1990 assignment agreements; their prior consent to the assignments was supplied by operation of the assignment clause in the original 1917 lease. Nor do Respondents dispute that

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[2] The 1996 amendment also added the following sentence to Section 5118(d)(2): "Nothing in the preceding sentence shall be construed to affect the enforceability of a Gold Clause contained in any obligation issued after October 27, 1977 if the enforceability of that Gold Clause has been finally adjudicated before the date of enactment of the Economic Growth and Regulatory Paperwork Reduction Act of 1996." Pub. L. No. 104-208, § 2609. Respondents do not dispute that this case had not been "finally adjudicated" before September 30, 1996.

neither Statesman nor Petitioner were even aware in 1990 that the original 1917 lease contained a gold clause. Finally, it is undisputed that Respondents themselves were not aware until 1991, long after the 1990 assignment agreement had been entered by Statesman and Petitioner, that Congress had legalized the use of gold clauses in post-1977 obligations. Indeed, for over three years after Respondents allegedly became entitled under the 1990 assignment agreement to demand payment in 1917 gold coins (which, in current dollars, amounts to an annual rent of approximately $460,000), Petitioner tendered, and Respondents accepted, monthly rental payments totaling $23,000 per year.

In the face of these undisputed facts, and while acknowledging that "the intent of the parties controls" the interpretation of a written agreement, the Eighth Circuit held that Petitioner was bound under the 1990 assignment agreement to make its rental payments in 1917 gold coins. The Eighth Circuit did not attempt to explain why Statesman, gratuitously and for no apparent reason, effectively raised its own annual rent obligation from $23,000 to approximately $460,000 by saddling its wholly-owned subsidiary with an obligation to pay rent in 1917 gold coins. Nor did the panel below attempt to explain why Respondents refrained for over three years from demanding the 20-fold increase in rent to which they were allegedly entitled.[3] Nor did the panel below

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[3] In their brief in opposition to certiorari, Respondents acknowledged that under their argument the obligation to pay rent in gold coins was actually created in 1985, when State Auto assigned the lease to Statesman. Opp. at 14 n.4. Respondents admit that they "had merely not invoked" their alleged right to

attempt to explain how the parties to the 1990 assignment agreement could have intended to obligate Petitioner to pay its rent in gold coins when none of the parties – Statesman, Petitioner, or Respondents – were even aware of the gold clause when the 1990 assignment agreement was entered.[4]

The 1996 amendment to Section 5118(d)(2), which was enacted less than two months after the Eighth Circuit's decision in this case, was specifically aimed at preventing precisely the result reached by the panel below. Designed to "ensure[ ] that the old gold clauses apply only when such a clause is the *explicit intention* of both parties to the contract," 142 Cong. Rec. H4755 (emphasis added), the amendment prohibits the enforcement of gold clauses in pre-1977 obligations, "notwithstanding any assignment or novation of such obligation

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insist on a 20-fold increase in rent, *id.*, but offer no explanation for, in effect, donating approximately $437,000 per year to their tenant for over eight years. Respondents' failure to explain their generosity exposes the transparently contrived nature of their claim. The truth, of course, is that the parties to the 1985 and the 1990 assignment agreements did not create an obligation to pay rent under the lease in gold coins.

[4] Respondents' claim that the 1990 assignment agreement "was an arm's length transaction between two corporate entities with extensive business expertise" and formed with "the advice of sophisticated legal counsel." Opp. at 14. In truth, however, the transaction was between the parent corporation (Statesman) and its wholly owned subsidiary (Petitioner), and it was entered, as the district court found, purely "for reasons internal to the organization of Statesman." Appendix to Petition for a Writ of Certiorari ("App.") at 24a n.1. In any event, the key point, which Respondents do not dispute, *see* Opp. at 14-15, is that neither Statesman nor Petitioner genuinely intended to revive the gold clause in the 1990 assignment agreement.

after October 27, 1977, unless all parties to the assignment or novations specifically agree to include a gold clause in the new agreement." Pub. L. No. 104-208, § 2609. Respondents argue that the Eighth Circuit's decision below conforms to the requirements of the 1996 amendment, noting that the Court of Appeals found that the original 1917 lease had been incorporated by reference into the 1990 assignment agreement and that Petitioner had thus "*specifically agreed* to be bound by the obligation described in the 1917 lease and its written amendments." Opp. at 16, quoting App. at 15a. But the 1996 amendment specifically provides that a standard assignment or novation incorporating the terms, including a gold clause, of a pre-1977 obligation is not enough. Indeed, the *unintentional* revival of a gold clause through the assignment or novation of a pre-1977 obligation is precisely – *precisely* – what Congress sought to prevent in amending Section 5118(d)(2). Thus, Congress expressly provided that a gold clause is unenforceable unless it was specifically negotiated and agreed to by all parties to the assignment or novation of the pre-1977 obligation. Here, as previously noted, Respondents admit that neither Statesman, nor Petitioner, nor even Respondents themselves, even *considered* the gold clause in connection with the 1990 assignment agreement, let alone intended to revive it. The Eighth Circuit acknowledged this fact as well. *See* App. 9a, 11a. Accordingly, because none of the relevant parties specifically agreed to include a gold clause in the 1990 assignment agreement, it is clear that Congress' recent amendment to Section 5118(d)(2) applies to this case and that Petitioner cannot be required to pay its rent in gold coins.

Respondents also argue that if we are correct concerning the applicability to this case of the 1996 amendment to Section 5118(d)(2), "then every other provision of the lease agreement between American Life and the Trostel heirs is voidable at American Life's fancy." Opp. at 16. The only provision of the lease agreement, however, governed by Section 5118(d)(2) is the gold clause, and it has been governed by federal law since 1933. Obviously, no other term of the lease is embraced by our argument concerning Section 5118(d)(2).

Finally, Respondents argue that even if the 1996 amendment to Section 5118(d)(2) governs this case, the Eighth Circuit's "misapplication . . . of law" is too narrow and unimportant to warrant this Court's review. Opp. at 17-18. The Eighth Circuit, however, did not misapply the 1996 amendment; the amendment was not enacted until two months after the Eighth Circuit rendered its decision. Accordingly, because the Court of Appeals did not consider this intervening and plainly dispositive legislation, this case is a textbook occasion for the Court to grant the petition, vacate the judgment below, and remand the case for reconsideration in light of the 1996 amendment to Section 5118(d)(2). *See, e.g., Bureau of Econ. Analysis v. Long*, 454 U.S. 934 (1981); R. Stern, E. Gressman, S. Shapiro & K. Geller, *Supreme Court Practice* 249 (7th ed. 1993). Alternatively, the Court should grant the petition and set this case for plenary review. As discussed in the petition (and below), the Eighth Circuit's decision below conflicts with the reasoning of a recent Ninth Circuit decision involving gold clauses in railroad bonds. Pet. at 24-26. The logic of the decision below cannot reasonably be confined to pre-1933 leases, but extends as well to gold

bonds and other long-term instruments containing gold clauses. Indeed, the issue presented by this case was deemed by Congress to be sufficiently important to enact a statute specifically resolving it. The correct application of that statute is, likewise, important enough to warrant this Court's review.

2. The brief in opposition to certiorari offers nothing to dispel the conclusion that the decision below conflicts directly with the Ninth Circuit's decision in *Adams v. Burlington N. R.R. Co.*, 80 F.3d 1377 (9th Cir.), *cert. denied*, 117 S. Ct. 171 (U.S. Oct. 7, 1996). Respondents emphasize that the Ninth Circuit in *Adams* rejected the bondholders' claim that "a novation occurred each time railroad bonds were sold." Opp. at 8. Respondents ignore, however, that the Ninth Circuit in *Adams* also rejected the bondholders' claim that a 1992 supplemental indenture in which a third party, CSX Transportation, Inc., expressly assumed the obligation to repay the bonds "according to their tenor" constituted a post-1977 novation of the bond agreement that revived the gold clause contained in the original bond. *See Adams*, 80 F.3d at 1382.

The central fact, therefore, in both *Adams* and the instant case is that a contracting party's rights and obligations were transferred after 1977 to a third party in an agreement that incorporated the terms of the original instrument, including a gold clause, by reference. Yet, the two courts of appeals came to precisely opposite conclusions as to the enforceability of the gold clauses. Apart from a conclusory assertion that leases and bonds are not "comparable," Respondents make no effort to explain the conflicting results reached in the two cases. Opp. at 8. We respectfully submit that the Ninth Circuit in *Adams* got it

right and that this Court should grant certiorari to resolve the conflict and to correct the Eighth Circuit's decision.

CONCLUSION

For the foregoing reasons, and those stated in the petition, this Court should grant the petition for a writ of certiorari, vacate the judgment of the Court of Appeals, and remand the case for reconsideration in light of the 1996 amendment to 31 U.S.C. § 5118(d)(2). Alternatively, the petition should be granted and the case set for plenary review.

Respectfully submitted,

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